

McKibben
Redwine
DeLuery

SSB-1254

Ways & Means
Succeeded By

SENATE FILE / HF 521
BY (PROPOSED COMMITTEE ON
WAYS AND MEANS BILL BY
CHAIRPERSON MCKIBBEN)

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

A BILL FOR

1 An Act establishing a new economy employment initiative by
2 providing for a partial deduction under the individual income
3 tax for the capital gain from the sale or exchange of capital
4 stock of a corporation which was acquired by an individual on
5 account of employment with the corporation, limiting the
6 fiscal impact of the partial deductions, and including an
7 effective and retroactive applicability date provision.

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

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1 Section 1. Section 422.7, Code 2001, is amended by adding
2 the following new subsection:

3 NEW SUBSECTION. 36. a. For purposes of this subsection:

4 (1) "Capital stock" means voting and nonvoting common and
5 preferred stock and stock options issued pursuant to an
6 incentive stock option plan. "Capital stock" does not include
7 stock rights, stock warrants, or debt securities, and does not
8 include stock or stock options issued by a corporation which
9 does not offer incentive stock options to all full-time
10 employees. A corporation does not offer incentive stock
11 options to all full-time employees unless each of those
12 employees is issued at least a number of incentive stock
13 options equal to twenty percent of all issued outstanding
14 incentive stock options divided by the number of full-time
15 employees.

16 (2) "Corporation" means any of the following:

17 (a) A corporation which at the time of the first sale or
18 exchange for which an election is made under paragraph "c" has
19 been in existence and actively doing business for at least
20 three years and is not a personal holding company as defined
21 in section 542(a) of the Internal Revenue Code.

22 (b) A corporation which is a member of an affiliated
23 group, as defined in section 1504(a) of the Internal Revenue
24 Code, which group includes a corporation described in
25 subparagraph subdivision (a) and which group has been in
26 existence and actively doing business for at least three
27 years.

28 (c) A predecessor or successor corporation of a
29 corporation described in subparagraph subdivision (a). A
30 corporation is a predecessor or successor corporation if the
31 corporation was a party to a reorganization that was entirely
32 or substantially income tax free and that occurred during or
33 after the employment of the taxpayer making an election under
34 paragraph "c".

35 (3) "Incentive stock option" means the same as defined in

1 section 422(b) of the Internal Revenue Code.

2 b. For purposes of this subsection, the corporation
3 issuing capital stock for which an election under paragraph
4 "c" is made must, at the time of the first sale or exchange
5 for which the election is made, have at least five
6 shareholders and at least two shareholders or groups of
7 shareholders who are not related to each other and each of
8 which owns at least five percent of the capital stock.

9 For purposes of this paragraph "b", two persons shall be
10 considered to be related when, under section 318 of the
11 Internal Revenue Code, one is a person who owns, directly or
12 indirectly, capital stock that if directly owned would be
13 attributed to the other person or is the spouse, child,
14 parent, grandparent, brother, sister, aunt, uncle, cousin,
15 niece, or nephew of the other person who owns capital stock
16 either directly or indirectly.

17 c. (1) In the manner provided in paragraph "d", an
18 individual may elect to subtract one-half of the capital gain
19 from the sale or exchange of capital stock of a corporation
20 acquired by the individual on account of employment with that
21 corporation. However, for tax years beginning in the 2001
22 calendar year, the amount that may be subtracted is one-fourth
23 of such capital gain.

24 (2) (a) Each individual shall be entitled to two
25 elections under subparagraph (1) during the individual's
26 lifetime for the capital stock of two different corporations.

27 (b) The election applies only to the tax year for which
28 the election was made and applies to all sales and exchanges
29 in the tax year for which the election was made of capital
30 stock in the same corporation which was acquired as provided
31 in subparagraph (1).

32 (c) After the individual makes an election for the tax
33 year, the election shall also apply to the sale or exchange in
34 that tax year of capital stock of the corporation which had
35 been transferred by inter vivos gift from the individual to

1 the individual's spouse if the capital stock was acquired as
2 provided in subparagraph (1). This provision applies in the
3 case of the spouse, only if the spouse was married to such
4 individual on the date of sale or exchange or the date of
5 death of the individual and if the spouse and individual file
6 a joint Iowa income tax return on which the election is made.
7 If the individual dies without making an election, the
8 surviving spouse may make the election for capital stock that
9 would have qualified under this subparagraph subdivision.

10 However, if there is no surviving spouse, the oldest surviving
11 issue who owns capital stock that would have qualified under
12 this subparagraph subdivision may make the election.

13 d. An election under paragraph "c" shall be made by
14 including a written statement with the taxpayer's Iowa income
15 tax return for the tax year for which the election is made.
16 The written statement shall identify the corporation that
17 issued the capital stock, the grounds for the election under
18 this subsection, and that the taxpayer elects to have this
19 subsection apply to sales and exchanges in that tax year.

20 (1) In order for the taxpayer to claim the benefits of the
21 partial deduction of the capital gain under this subsection,
22 the taxpayer must completely fill out the tax return,
23 determine the taxpayer's income tax liability without the
24 benefit of this subsection, and pay the amount of tax owed.
25 The taxpayer shall recompute the taxpayer's income tax
26 liability, by applying the provisions of this subsection on a
27 special return. This special return shall be filed under
28 rules of the director and constitutes a claim for refund of
29 the difference between the amount of tax the taxpayer paid as
30 determined without the application of the provisions of this
31 subsection and the amount of tax determined with the
32 application of the provisions of this subsection.

33 (2) This subsection shall not affect the amount of the
34 taxpayer's checkoff to the Iowa election campaign fund under
35 section 56.18, the checkoff for the state fish and game

1 protection fund in section 456A.16, the credits from tax
2 provided in sections 422.10, 422.11A, and 422.12 and the
3 allocation of these credits between spouses if the taxpayers
4 filed separate returns or separately on combined returns.

5 (3) For any tax year, the aggregate amount of refund
6 claims that shall be paid pursuant to this subsection shall
7 not exceed three million dollars. If, for a tax year, the
8 aggregate amount of refund claims filed pursuant to this
9 subsection exceeds three million dollars, each claim for
10 refund shall be paid on a pro rata basis so that the aggregate
11 amount of refund claims paid does not exceed three million
12 dollars. In the case where refund claims are not paid in
13 full, the amount of the refund to which the taxpayer is
14 entitled under this subsection is the pro rata amount that was
15 paid and the taxpayer is not entitled to a refund of the
16 unpaid portion and is not entitled to carry that amount
17 forward or backward to another tax year. Taxpayers shall not
18 use refunds as estimated payments for the succeeding tax year.
19 Taxpayers whose tax years begin on January 1 must file their
20 refund claims by October 31 of the calendar year following the
21 end of their tax years to be eligible for refunds. Taxpayers
22 whose tax years begin on a date other than January 1 must file
23 their refund claims by the end of the tenth month following
24 the end of their tax years to be eligible. The department
25 shall determine on February 1 of the second succeeding
26 calendar year if the total amount of claims for refund exceeds
27 three million dollars for the tax year. Notwithstanding any
28 other provision, interest shall not be due on any refund
29 claims that are paid by the last day of February of the second
30 succeeding calendar year. If the claim is not payable on
31 February 1 of the second succeeding calendar year, because the
32 taxpayer is a fiscal year filer, then the amount of the claim
33 allowed shall be in the same ratio as the refund claims
34 available on February 1 of the second succeeding calendar
35 year. These claims shall be funded by moneys appropriated for

1 payment of individual income tax refunds.

2 e. The deduction under this subsection is in lieu of any
3 deduction allowable under section 1202 of the Internal Revenue
4 Code for the capital gain from the sale or exchange of the
5 same capital stock.

6 Sec. 2. EFFECTIVE AND RETROACTIVE APPLICABILITY DATE.

7 This Act, being deemed of immediate importance, takes effect
8 upon enactment and applies retroactively to January 1, 2001,
9 for tax years beginning on or after that date.

10

EXPLANATION

11 This bill provides a deduction under the individual income
12 tax of 50 percent (25 percent for the 2001 tax year) of the
13 capital gain from the sale or exchange of capital stock of a
14 corporation acquired by the taxpayer on account of employment
15 with the corporation. The taxpayer must make an election to
16 take the deduction and the election only applies for that tax
17 year. The election is made by a written statement filed with
18 the department. In addition, the benefits of the deduction
19 are realized by means of a refund claim. This involves the
20 taxpayer filing a return with tax liability determined without
21 deduction for the capital gain and a special return with tax
22 liability determined with the deduction for the capital gain.
23 The reduction in tax liability will be treated as a claim for
24 refund of the amount of the reduction. However, not more than
25 \$3 million in tax refunds may be allowed for any tax year. If
26 more refunds are claimed, then each refund claim is payable at
27 a pro rata amount, which is the final amount of the taxpayer's
28 actual refund. A taxpayer may make two elections for two
29 different corporations during the taxpayer's lifetime. The
30 election would also apply to stock sold during that tax year
31 which was previously granted to a spouse of the taxpayer but
32 only if they file a joint Iowa income tax return. The
33 election would not apply to capital gains from stock or stock
34 options unless the corporation issuing the options offered
35 them to all full-time employees.

1 The deduction is in lieu of the deduction that may be
2 allowable under the Internal Revenue Code for sale or exchange
3 of stock in a small business held for five years.

4 The bill takes effect upon enactment and applies
5 retroactively to January 1, 2001, for tax years beginning on
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Substitutes for HF 710
5/2/01
(P. 1728)

PRINTED

FILED APR 16 '01

SENATE FILE 521

BY COMMITTEE ON WAYS AND MEANS

(SUCCESSOR TO SSB 1254)

Passed Senate, ^(P. 1354) Date 4/26/01 Passed House, ^(P. 1730) Date 5/2/01
Vote: Ayes 28 Nays 20 Vote: Ayes 61 Nays 36
Approved 5/31/01
Vetted

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SF 521

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29 the difference between the amount of tax the taxpayer paid as
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24 refund of the amount of the reduction. However, not more than
25 \$3 million in tax refunds may be allowed for any tax year. If
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27 a pro rata amount, which is the final amount of the taxpayer's
28 actual refund. A taxpayer may make two elections for two
29 different corporations during the taxpayer's lifetime. The
30 election would also apply to stock sold during that tax year
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32 only if they file a joint Iowa income tax return. The
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34 options unless the corporation issuing the options offered
35 them to all full-time employees.

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4 The bill takes effect upon enactment and applies
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SENATE FILE 521

S-3442

1 Amend Senate File 521 as follows:

2 1. Page 5, by striking lines 6 through 9 and
3 inserting the following:

4 "Sec. ____ EFFECTIVE AND RETROACTIVE APPLICABILITY
5 PROVISION. This Act takes effect only if the revenue
6 estimating conference estimates that, as a result of
7 the enactment of federal income tax legislation prior
8 to January 1, 2002, Iowa income tax receipts for the
9 fiscal year beginning July 1, 2001, will be increased
10 by \$7.9 million or more over the amount of Iowa income
11 tax receipts which would have been realized in the
12 absence of the enactment of such federal income tax
13 legislation. If this Act takes effect, this Act
14 applies retroactively to January 1, 2001, for tax
15 years beginning on or after that date."

W/D 4/26/01 (P1353)

By LARRY MCKIBBEN

S-3442 FILED APRIL 23, 2001

SENATE FILE 521

S-3537

1 Amend Senate File 521 as follows:

2 1. By striking page 4, line 32 through page 5,
3 line 1, and inserting the following: "taxpayer is a
4 fiscal year filer, the claim shall be considered as a
5 claim for the following tax year."

By LARRY MCKIBBEN

S-3537 FILED APRIL 26, 2001

ADOPTED

(P1353)

SENATE FILE 521

S-3541

1 Amend the amendment, S-3442, to Senate File 521 as
2 follows:

3 1. Page 1, line 4, by striking the word
4 "RETROACTIVE".

5 2. Page 1, by striking lines 14 and 15 and
6 inserting the following: "applies to tax years
7 beginning on or after January 1, 2003."

8 ____ Title page, line 7, by striking the word
9 "retroactive".

By THOMAS FIEGEN

S-3541 FILED APRIL 26, 2001

RULED OUT OF ORDER

(P1353)

**SENATE FILE 521
FISCAL NOTE**

A fiscal note for **Senate File 521 as amended by S-3537** 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 521 as amended by S-3537 provides for a 50.0% (25.0% in tax year 2001) deduction from taxable income of the capital gain from the sale or exchange of stock of a corporation when the stock was acquired on account of employment with the corporation. A taxpayer is limited to two deductions for the stock of two corporations during the taxpayers lifetime. The total State cost for all such deductions is limited to \$3.0 million per year. If the claims exceed \$3.0 million, the tax benefits are prorated. The Bill takes effect upon enactment and applies to 2001 and subsequent tax years. The Department of Revenue and Finance is directed to determine by February 1 the total value of all refund claims from returns filed in the previous calendar year. Therefore, refunds for tax year 2001 will be paid after February 1 of calendar year 2003 (fiscal year 2003).

BACKGROUND

The income deduction in Senate File 521 as amended by S-3537 would be available for stock acquired by employees and owners of companies when the stock was acquired through a qualified employee stock option plan and also for stock acquired by company owners when the corporation was created (founder's shares).

The capital gain on stock acquired through an employee stock option plan would be equal to the difference between the price of the stock when sold and the price of the stock when the option was granted. For example, if an employee is granted 1,000 stock option shares when the share value of the company is \$15 and then exercises the option when the value is \$50 per share, the person would have a capital gain equal to \$35,000 (\$50 received minus \$15 paid times 1,000 shares). The Bill would reduce the taxpayer's Iowa income tax by approximately \$1,200 to \$1,600, depending on the employee's marginal tax rate.

The capital gain on stock received as founder's shares would in most instances be equal to the price received when the stock is sold or exchanged. This is because stock issued at a company's founding has no market-determined value. If 1,000 shares of stock are sold at \$50 per share, the capital gain would be \$50,000 (\$50 received times 1,000 shares). The Bill would reduce the taxpayer's Iowa income tax by \$2,250 at the maximum 8.99% marginal tax rate.

The above numbers are examples for illustrative purposes only. The benefit to individual taxpayer's would be determined by the number of shares received, the price paid per share for the option, and the price received when the option share is sold.

FISCAL IMPACT

.EJECT

SENATE CLIP SHEET

APRIL 27, 2001

Page 27

PAGE 2 , FISCAL NOTE, SENATE FILE 521

refunds not being paid before February 1, 2003. As a result of the Bill becoming effective more than one-third of the way through tax year 2001 and the benefit for tax year 2001 is only one-half the benefit in future fiscal years, the value of tax refunds paid in FY 2003 will be \$1.0 million of the \$3.0 million available. The fiscal impact in FY 2004 and beyond is estimated to be \$3.0 million per year.

SOURCES

Legislative Fiscal Bureau analysis
Department of Revenue and Finance analysis

(LSB 3150SV.2, JWR)

FILED APRIL 26, 2001

BY DENNIS PROUTY, FISCAL DIRECTOR

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2 the following new subsection:

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33 year, the election shall also apply to the sale or exchange in
34 that tax year of capital stock of the corporation which had
35 been transferred by inter vivos gift from the individual to

1 the individual's spouse if the capital stock was acquired as
2 provided in subparagraph (1). This provision applies in the
3 case of the spouse, only if the spouse was married to such
4 individual on the date of sale or exchange or the date of
5 death of the individual and if the spouse and individual file
6 a joint Iowa income tax return on which the election is made.
7 If the individual dies without making an election, the
8 surviving spouse may make the election for capital stock that
9 would have qualified under this subparagraph subdivision.

10 However, if there is no surviving spouse, the oldest surviving
11 issue who owns capital stock that would have qualified under
12 this subparagraph subdivision may make the election.

13 d. An election under paragraph "c" shall be made by
14 including a written statement with the taxpayer's Iowa income
15 tax return for the tax year for which the election is made.
16 The written statement shall identify the corporation that
17 issued the capital stock, the grounds for the election under
18 this subsection, and that the taxpayer elects to have this
19 subsection apply to sales and exchanges in that tax year.

20 (1) In order for the taxpayer to claim the benefits of the
21 partial deduction of the capital gain under this subsection,
22 the taxpayer must completely fill out the tax return,
23 determine the taxpayer's income tax liability without the
24 benefit of this subsection, and pay the amount of tax owed.
25 The taxpayer shall recompute the taxpayer's income tax
26 liability, by applying the provisions of this subsection on a
27 special return. This special return shall be filed under
28 rules of the director and constitutes a claim for refund of
29 the difference between the amount of tax the taxpayer paid as
30 determined without the application of the provisions of this
31 subsection and the amount of tax determined with the
32 application of the provisions of this subsection.

33 (2) This subsection shall not affect the amount of the
34 taxpayer's checkoff to the Iowa election campaign fund under
35 section 56.18, the checkoff for the state fish and game

1 protection fund in section 456A.16, the credits from tax
2 provided in sections 422.10, 422.11A, and 422.12 and the
3 allocation of these credits between spouses if the taxpayers
4 filed separate returns or separately on combined returns.

5 (3) For any tax year, the aggregate amount of refund
6 claims that shall be paid pursuant to this subsection shall
7 not exceed three million dollars. If, for a tax year, the
8 aggregate amount of refund claims filed pursuant to this
9 subsection exceeds three million dollars, each claim for
10 refund shall be paid on a pro rata basis so that the aggregate
11 amount of refund claims paid does not exceed three million
12 dollars. In the case where refund claims are not paid in
13 full, the amount of the refund to which the taxpayer is
14 entitled under this subsection is the pro rata amount that was
15 paid and the taxpayer is not entitled to a refund of the
16 unpaid portion and is not entitled to carry that amount
17 forward or backward to another tax year. Taxpayers shall not
18 use refunds as estimated payments for the succeeding tax year.
19 Taxpayers whose tax years begin on January 1 must file their
20 refund claims by October 31 of the calendar year following the
21 end of their tax years to be eligible for refunds. Taxpayers
22 whose tax years begin on a date other than January 1 must file
23 their refund claims by the end of the tenth month following
24 the end of their tax years to be eligible. The department
25 shall determine on February 1 of the second succeeding
26 calendar year if the total amount of claims for refund exceeds
27 three million dollars for the tax year. Notwithstanding any
28 other provision, interest shall not be due on any refund
29 claims that are paid by the last day of February of the second
30 succeeding calendar year. If the claim is not payable on
31 February 1 of the second succeeding calendar year, because the
32 taxpayer is a fiscal year filer, the claim shall be considered
33 as a claim for the following tax year.

34 e. The deduction under this subsection is in lieu of any
35 deduction allowable under section 1202 of the Internal Revenue

1 Code for the capital gain from the sale or exchange of the
2 same capital stock.

3 Sec. 2. EFFECTIVE AND RETROACTIVE APPLICABILITY DATE.

4 This Act, being deemed of immediate importance, takes effect
5 upon enactment and applies retroactively to January 1, 2001,
6 for tax years beginning on or after that date.

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SENATE FILE 521

H-1831

1 Amend Senate File 521, as amended, passed, and
2 reprinted by the Senate, as follows:

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

5 "Section 1. NEW SECTION. 15E.221 SHORT TITLE.

6 This division shall be known and may be cited as
7 the "Financial Capital Formation for Life Science
8 Companies Program".

9 Sec. ____ . NEW SECTION. 15E.222 DEFINITIONS.

10 As used in this division, unless the context
11 otherwise requires:

12 1. "Equity" means common stock or preferred stock,
13 regardless of class or series, of a corporation; a
14 partnership interest in a limited partnership; or a
15 membership interest in a limited liability company,
16 which is not required or subject to an option on the
17 part of the taxpayer to be redeemed by the issuer
18 within two years from the date of issuance.

19 2. "Qualified business" means a business that
20 meets all of the following criteria:

21 a. Has annual gross revenues of five million
22 dollars or less in its most recent fiscal year.

23 b. Is domiciled in the state of Iowa.

24 c. Is engaged in business primarily in, or does
25 substantially all of its production in, the state of
26 Iowa.

27 d. Is primarily engaged in a business that
28 produces, develops, or markets a life science product
29 or life science by-product as defined in section
30 10C.1.

31 3. "Subordinated debt" means debt that either is
32 unsecured or has a subordinate claim on the assets of
33 the debtor.

34 Sec. ____ . NEW SECTION. 15E.223 TAX CREDITS.

35 1. For tax years beginning on or after January 1,
36 2001, a tax credit shall be allowed against the taxes
37 imposed under chapter 422, divisions II, III, and V,
38 and under chapter 432, for a certified equity or
39 subordinated debt investment in a qualified business.
40 An individual may claim the credit of a partnership,
41 limited liability company, S corporation, estate, or
42 trust electing to have income taxed directly to the
43 individual. The amount claimed by the individual
44 shall be based upon the pro rata share of the
45 individual's earnings from the partnership, limited
46 liability company, S corporation, estate, or trust.

47 2. a. The tax credit allowed under this section
48 shall be for the following amounts:

49 (1) After the certified equity or subordinated
50 debt investment is held for a period of two years,

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1 twenty percent of the certified equity or subordinated
2 debt investment.

3 (2) After the certified equity or subordinated
4 debt investment is held for a period of four years, an
5 additional ten percent of the certified equity or
6 subordinated debt investment.

7 (3) After the certified equity or subordinated
8 debt investment is held for a period of six years, an
9 additional ten percent of the certified equity or
10 subordinated debt investment.

11 (4) After the certified equity or subordinated
12 debt investment is held for a period of eight years,
13 an additional ten percent of the certified equity or
14 subordinated debt investment.

15 b. For purposes of paragraph "a" in computing the
16 holding period of an equity investment that was
17 obtained by the taxpayer as a result of the conversion
18 of the taxpayer's investment in a subordinated debt,
19 the time the taxpayer held the investment in the
20 subordinated debt shall be added to the time the
21 taxpayer held the equity investment.

22 c. Any tax credit in excess of the taxpayer's
23 liability for the tax year may be credited to the tax
24 liability for the following three years or until
25 depleted, whichever is earlier. A tax credit shall
26 not be carried back to a tax year prior to the tax
27 year in which the taxpayer redeems the tax credit.

28 d. A taxpayer shall not claim a tax credit in a
29 single tax year under this section of more than fifty
30 thousand dollars.

31 e. A taxpayer making an equity or subordinated
32 debt investment in a qualified business shall submit
33 an application to the department of economic
34 development for certification of eligibility for a tax
35 credit.

36 3. The aggregate amount of tax credits issued
37 under this section for taxes imposed pursuant to
38 chapter 422, divisions II, III, and V, and chapter 432
39 shall not exceed a total of three million dollars.

40 4. The department of revenue and finance, in
41 consultation with the department of economic
42 development, shall develop a system for registration,
43 authorization, and redemption of tax credits issued by
44 the state under this section. The department of
45 revenue and finance and the department of economic
46 development shall adopt any other policies,
47 procedures, or rules pursuant to chapter 17A necessary
48 for the administration of this section and of tax
49 credits issued by the state under this section.

50 Sec. ____ . NEW SECTION. 422.11C LIFE SCIENCE TAX

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1 CREDIT.

2 The taxes imposed under this division, less the
3 credits allowed under section 422.12 and any other
4 nonrefundable credit, shall be reduced by a tax credit
5 in the manner as authorized pursuant to section
6 15E.223.

7 Sec. _____. Section 422.33, Code 2001, is amended by
8 adding the following new subsection:

9 NEW SUBSECTION. 11. The taxes imposed under this
10 division shall be reduced by a tax credit in the
11 manner as authorized pursuant to section 15E.223.

12 Sec. _____. Section 422.60, Code 2001, is amended by
13 adding the following new subsection:

14 NEW SUBSECTION. 4. The taxes imposed under this
15 division shall be reduced by a tax credit in the
16 manner as authorized pursuant to section 15E.223.

17 Sec. _____. NEW SECTION. 432.12A LIFE SCIENCE TAX
18 CREDIT.

19 The taxes imposed under this chapter shall be
20 reduced by a tax credit in the manner as authorized
21 pursuant to section 15E.223."

22 2. Title page, by striking lines 1 through 7, and
23 inserting the following: "An Act creating a tax
24 credit for investments in qualified businesses engaged
25 in life science-related production."

26 3. By renumbering as necessary.

By WARNSTADT of Woodbury

H-1831 FILED MAY 1, 2001

W/D

5/2/01

(P 1729)

SENATE FILE 521

H-1864

1 Amend Senate File 521, as amended, passed, and
2 reprinted by the Senate, as follows:

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

5 "Section 1. There is appropriated from the general
6 fund of the state to the designated entities for the
7 fiscal year beginning July 1, 2001, and ending June
8 30, 2002, the following amounts to be used for the
9 purposes designated:

- 10 1. To the department of human services for use in
11 the HAWK-I program:
12 \$ 1,707,951
- 13 2. To the Iowa department of public health for
14 childhood immunizations:
15 \$ 160,618
- 16 3. To the Iowa department of public health for
17 child and adolescent wellness:
18 \$ 167,918
- 19 4. To the Iowa department of public health for
20 community capacity:
21 \$ 182,520
- 22 5. To the department of workforce development for
23 rural workforce development offices:
24 \$ 780,000

25 The appropriations made in this section are in
26 addition to appropriations made in other Acts for the
27 designated purposes.

28 Sec. 2. EFFECTIVE PROVISION. This Act takes
29 effect only if the revenue estimating conference
30 estimates that, as a result of the enactment of
31 federal income tax legislation prior to January 1,
32 2002, Iowa income tax receipts for the fiscal year
33 beginning July 1, 2001, will be increased by \$7.9
34 million or more over the amount of Iowa income tax
35 receipts which would have been realized in the absence
36 of the enactment of such federal income tax
37 legislation."

38 2. Title page, by striking lines 1 through 7, and
39 inserting the following: "An Act making
40 appropriations to the departments of human services,
41 workforce development, and public health and including
42 a contingent effective date provision."

By KREIMAN of Davis

H-1864 FILED MAY 1, 2001

w/d
5/2/01
(p. 1729)



THOMAS J. VILSACK
GOVERNOR

OFFICE OF THE GOVERNOR

SALLY J. PEDERSON
LT. GOVERNOR

May 31, 2001

The Honorable Chester Culver
Secretary of State
State Capitol
LOCAL

MAY 31 2001

Dear Secretary Culver:

I hereby transmit Senate File 521, an Act establishing a new economy employment initiative by providing for a partial deduction under the individual income tax for the capital gain from the sale or exchange of capital stock of a corporation which was acquired by an individual on account of employment with the corporation, limiting the fiscal impact of the partial deductions, and including an effective and retroactive applicability date provision.

I am unable to approve Senate File 521. At the start of the legislative session, I identified the need to help attract venture capital for business start-ups in Iowa. My recommendations focused in the life sciences area, where I feel the best opportunities exist attracting venture capital. Unfortunately, the Legislature felt that this was not a top priority for this session. Instead, they passed Senate File 521, which provides a tax advantage to individuals in dealing with capital gains on the sale of stock in corporations. While providing this advantage to help corporations hire and retain workers, my emphasis has been and will continue to be creating the appropriate atmosphere for which these businesses can be created. Creating venture capital for the state needs to be the first step.

Also, because of the state's future financial uncertainty, approving this bill would not be responsible. It is important to remember that in fiscal year 2002, the Legislature chose to fund many on-going operating expenses

with one-time revenues. Finding new revenue sources in fiscal year 2003 for these operating expenses will be difficult. Signing this bill would add to that difficulty.

For the above reasons, I hereby respectfully disapprove Senate File 521.

Sincerely,

A handwritten signature in black ink, appearing to read "Tom Vilsack", written in a cursive style.

Thomas J. Vilsack
Governor

TJV:jmc

CC: Secretary of the Senate
Chief Clerk of the House

SENATE FILE 521

AN ACT

ESTABLISHING A NEW ECONOMY EMPLOYMENT INITIATIVE BY PROVIDING FOR A PARTIAL DEDUCTION UNDER THE INDIVIDUAL INCOME TAX FOR THE CAPITAL GAIN FROM THE SALE OR EXCHANGE OF CAPITAL STOCK OF A CORPORATION WHICH WAS ACQUIRED BY AN INDIVIDUAL ON ACCOUNT OF EMPLOYMENT WITH THE CORPORATION, LIMITING THE FISCAL IMPACT OF THE PARTIAL DEDUCTIONS, AND INCLUDING AN EFFECTIVE AND RETROACTIVE APPLICABILITY DATE PROVISION.

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

Section 1. Section 422.7, Code 2001, is amended by adding the following new subsection:

NEW SUBSECTION. 36. a. For purposes of this subsection:

(1) "Capital stock" means voting and nonvoting common and preferred stock and stock options issued pursuant to an incentive stock option plan. "Capital stock" does not include stock rights, stock warrants, or debt securities, and does not include stock or stock options issued by a corporation which does not offer incentive stock options to all full-time employees. A corporation does not offer incentive stock options to all full-time employees unless each of those employees is issued at least a number of incentive stock options equal to twenty percent of all issued outstanding incentive stock options divided by the number of full-time employees.

(2) "Corporation" means any of the following:

(a) A corporation which at the time of the first sale or exchange for which an election is made under paragraph "c" has been in existence and actively doing business for at least three years and is not a personal holding company as defined in section 542(a) of the Internal Revenue Code.

(b) A corporation which is a member of an affiliated group, as defined in section 1504(a) of the Internal Revenue Code, which group includes a corporation described in subparagraph subdivision (a) and which group has been in existence and actively doing business for at least three years.

(c) A predecessor or successor corporation of a corporation described in subparagraph subdivision (a). A corporation is a predecessor or successor corporation if the corporation was a party to a reorganization that was entirely or substantially income tax free and that occurred during or after the employment of the taxpayer making an election under paragraph "c".

(3) "Incentive stock option" means the same as defined in section 422(b) of the Internal Revenue Code.

b. For purposes of this subsection, the corporation issuing capital stock for which an election under paragraph

"c" is made must, at the time of the first sale or exchange for which the election is made, have at least five shareholders and at least two shareholders or groups of shareholders who are not related to each other and each of which owns at least five percent of the capital stock.

For purposes of this paragraph "b", two persons shall be considered to be related when, under section 318 of the Internal Revenue Code, one is a person who owns, directly or indirectly, capital stock that if directly owned would be attributed to the other person or is the spouse, child, parent, grandparent, brother, sister, aunt, uncle, cousin, niece, or nephew of the other person who owns capital stock either directly or indirectly.

c. (1) In the manner provided in paragraph "d", an individual may elect to subtract one-half of the capital gain from the sale or exchange of capital stock of a corporation acquired by the individual on account of employment with that corporation. However, for tax years beginning in the 2001 calendar year, the amount that may be subtracted is one-fourth of such capital gain.

(2) (a) Each individual shall be entitled to two elections under subparagraph (1) during the individual's lifetime for the capital stock of two different corporations.

(b) The election applies only to the tax year for which the election was made and applies to all sales and exchanges in the tax year for which the election was made of capital stock in the same corporation which was acquired as provided in subparagraph (1).

(c) After the individual makes an election for the tax year, the election shall also apply to the sale or exchange in that tax year of capital stock of the corporation which had been transferred by inter vivos gift from the individual to the individual's spouse if the capital stock was acquired as provided in subparagraph (1). This provision applies in the case of the spouse, only if the spouse was married to such

individual on the date of sale or exchange or the date of death of the individual and if the spouse and individual file a joint Iowa income tax return on which the election is made. If the individual dies without making an election, the surviving spouse may make the election for capital stock that would have qualified under this subparagraph subdivision. However, if there is no surviving spouse, the oldest surviving issue who owns capital stock that would have qualified under this subparagraph subdivision may make the election.

d. An election under paragraph "c" shall be made by including a written statement with the taxpayer's Iowa income tax return for the tax year for which the election is made. The written statement shall identify the corporation that issued the capital stock, the grounds for the election under this subsection, and that the taxpayer elects to have this subsection apply to sales and exchanges in that tax year.

(1) In order for the taxpayer to claim the benefits of the partial deduction of the capital gain under this subsection, the taxpayer must completely fill out the tax return, determine the taxpayer's income tax liability without the benefit of this subsection, and pay the amount of tax owed. The taxpayer shall recompute the taxpayer's income tax liability, by applying the provisions of this subsection on a special return. This special return shall be filed under rules of the director and constitutes a claim for refund of the difference between the amount of tax the taxpayer paid as determined without the application of the provisions of this subsection and the amount of tax determined with the application of the provisions of this subsection.

(2) This subsection shall not affect the amount of the taxpayer's checkoff to the Iowa election campaign fund under section 56.18, the checkoff for the state fish and game protection fund in section 456A.16, the credits from tax provided in sections 422.10, 422.11A, and 422.12 and the allocation of these credits between spouses if the taxpayers filed separate returns or separately on combined returns.

(3) For any tax year, the aggregate amount of refund claims that shall be paid pursuant to this subsection shall not exceed three million dollars. If, for a tax year, the aggregate amount of refund claims filed pursuant to this subsection exceeds three million dollars, each claim for refund shall be paid on a pro rata basis so that the aggregate amount of refund claims paid does not exceed three million dollars. In the case where refund claims are not paid in full, the amount of the refund to which the taxpayer is entitled under this subsection is the pro rata amount that was paid and the taxpayer is not entitled to a refund of the unpaid portion and is not entitled to carry that amount forward or backward to another tax year. Taxpayers shall not use refunds as estimated payments for the succeeding tax year. Taxpayers whose tax years begin on January 1 must file their refund claims by October 31 of the calendar year following the end of their tax years to be eligible for refunds. Taxpayers whose tax years begin on a date other than January 1 must file their refund claims by the end of the tenth month following the end of their tax years to be eligible. The department shall determine on February 1 of the second succeeding calendar year if the total amount of claims for refund exceeds three million dollars for the tax year. Notwithstanding any other provision, interest shall not be due on any refund claims that are paid by the last day of February of the second succeeding calendar year. If the claim is not payable on February 1 of the second succeeding calendar year, because the taxpayer is a fiscal year filer, the claim shall be considered as a claim for the following tax year.

e. The deduction under this subsection is in lieu of any deduction allowable under section 1202 of the Internal Revenue Code for the capital gain from the sale or exchange of the same capital stock.

Sec. 2. EFFECTIVE AND RETROACTIVE APPLICABILITY DATE.
This Act, being deemed of immediate importance, takes effect

upon enactment and applies retroactively to January 1, 2001, for tax years beginning on or after that date.

MARY E. KRAMER
President of the Senate

BRENT SIEGRIST
Speaker of the House

I hereby certify that this bill originated in the Senate and is known as Senate File 521, Seventy-ninth General Assembly.

MICHAEL E. MARSHALL
Secretary of the Senate

Vetoed
Approved 5/31, 2001

THOMAS J. VILSACK
Governor