

SALT Alert!



SALT Alert! 2018-07: Iowa Tax Reform Bill Pending Signature

In the last few hours of the regular 2018 legislative session, Iowa lawmakers passed an estimated \$2.1 billion tax cut to take place over the next several years. The legislation, [Senate File 2417](#), is currently pending signature by Governor Kim Reynolds. While many of the tax cuts are aimed at individuals, the bill also makes certain corporate changes and significantly revises the state's sales and use tax laws. These changes, including the effective dates, are described below.

Internal Revenue Code Conformity

Under current Iowa law, the definition of the Internal Revenue Code for individual income, corporate, and franchise tax purposes is the Internal Revenue Code of 1986 as amended to and including January 1, 2015. For tax years beginning during the 2019 calendar year, Senate File 2417 amends the definition of "Internal Revenue Code" to mean the Internal Revenue Code of 1986 as amended and in effect on March 24, 2018. For tax years beginning on or after January 1, 2020, "Internal Revenue Code" means the Internal Revenue Code of 1986, as amended. It appears, therefore, that Iowa will not adopt any tax reform changes enacted as part of the Tax Cuts and Jobs Act until the 2019 tax year when the state adopts the Code as of March 24, 2018. Senate File 2417 also provides that for tax years beginning on or after January 1, 2020, Iowa will no longer be a fixed-date state and will adopt the Internal Revenue Code as in effect for the tax year at issue.

Deduction for Qualified Business Income

Although the focus of this Alert is on corporate changes, one change affects businesses operating in pass-through form. Specifically, Senate File 2417 phases-in the ability, for Iowa individual income tax purposes, to take the deduction allowed under IRC section 199A for qualified business income. For tax years beginning on or after January 1, 2019, but before January 1, 2021, 25 percent of the deduction is allowed. That amount increases to 50 percent for tax years beginning during the 2021 calendar year, and to 75 percent for tax years beginning on or after January 1, 2022.

Corporate Rate Reduction

Under current law, the highest marginal corporate income tax rate is 12 percent. Senate File 2417 revises the corporate rate structure (beginning in 2021), as follows:

- On the first \$25,000 of taxable income the rate is 6 percent for tax years beginning prior to January 1, 2021 and the rate is 5.5 percent for tax years beginning on or after January 1, 2021;
- On taxable income between \$25,000 and \$100,000 or any part thereof, the rate is 8 percent for tax years beginning prior to January 1, 2021 and the rate is 5.5 percent for tax years beginning on or after January 1, 2021;
- On taxable income between \$100,000 and \$250,000 or any part thereof, the rate is 10 percent for tax years beginning prior to January 1, 2021 and the rate is 9 percent for tax years beginning on or after January 1, 2021;
- On taxable income of \$250,000 or more, the rate is 12 percent for tax years beginning prior to January 1, 2021 and the rate is 9.8 percent for tax years beginning on or after January 1, 2021.

Repeal of the Corporate Alternative Minimum Tax

Senate File 2417 repeals the corporate alternative minimum tax, which is equal to sixty percent of the maximum state corporate income tax rate, rounded to the nearest one-tenth of one percent, applied to the state alternative minimum taxable income of the taxpayer computed under Iowa law. The repeal is effective for tax years beginning on or after January 1, 2021. However, in computing state alternative minimum taxable income (before the repeal), the definition of Internal Revenue Code means the Internal Revenue Code of 1986 as amended and in effect on December 21, 2017.

Repeal of the Corporate Deduction for Federal Taxes Paid

Under Iowa Code § 422.35(4)(a), which is in the section of Iowa law addressing the computation of a corporation's net income, a taxpayer is allowed a deduction for fifty percent of the federal taxes paid or accrued, adjusted by any federal income tax refunds. This statute has been revised to provide that this deduction is allowed only for tax years beginning before January 1, 2022 and applies only to the extent the federal tax payment is for a tax year beginning prior to January 1, 2021.

Sales and Use Tax Base Expansion

Senate File 2417 expands the sales tax base to include certain services not previously subject to sales and use tax, including:

- Personal transportation services, including taxis, driver service, ride sharing, and rides for hire (limousine services were already taxable under existing law)
- Photography and retouching services (which were previously taxable as tangible personal property)
- Storage of tangible or electronic files, documents, or other records
- Information services (defined as delivering or providing access to databases or subscriptions to information through any tangible or electronic medium)
- Services arising from or related to installing, maintaining, servicing, repairing, operating, upgrading, or enhancing specified digital products
- Video game services and tournaments, and
- Software as a service

With the exception of photography and retouching services, the tax base expansions take

effect on January 1, 2019. The provisions related to photography and retouching services take effect on July 1, 2018.

Senate File 2417 also clarifies that streaming video, video on-demand, and pay-per view are included in taxable pay television services. The bill states that this change is a conforming amendment consistent with current law, and takes effect immediately upon passage of the bill.

Another significant change to Iowa law is that the sales and use tax base is expanded to include specified digital products sold at retail in Iowa effective January 1, 2019. Specified digital products include electronically transferred digital audio-visual works, digital audio works, digital books, or “other digital products” (defined as greeting cards, images, video or electronic games or entertainment, news or information products, and computer software applications). The bill also creates exemptions for specified digital products, prewritten computer software, and certain enumerated services (file storage, information services, software as a service, and services related to specified digital products) that are furnished to a commercial enterprise for use exclusively by the commercial enterprise. Also exempted are specified digital products sold to a non-end user.

In addition, Senate File 2417 redefines the term “sale” to include transfers, exchanges, or barters on a subscription basis. A “subscription” includes the right or ability to access, receive, use, obtain, purchase, or otherwise acquire taxable items on a permanent or less than permanent basis, regardless of whether the person actually accesses, receives, uses, obtains, purchases, or otherwise acquires the item. These definitions are conforming amendments consistent with current law, and become effective immediately.

The term “lease” or “rental” is also redefined to include access to tangible personal property or specified digital products, effective immediately.

The definition of “use” is also amended to include access to tangible personal property or specified digital products, or any right or power over or access to the product or result of a service. It appears that the definition of use for use tax purposes does not become effective until January 1, 2019, which makes sense given that this date is when such goods become subject to sale tax.

Requirements for Remote Sellers, Marketplace Facilitators, and Referrers

For transactions occurring on or after January 1, 2019, Senate File 2417 provides that the following will be considered retailers maintaining a place of business in the state, subject to the requirement to collect and remit sales and use tax:

- A retailer that has gross revenue from Iowa sales of at least \$100,000 or that makes Iowa sales in 200 or more separate transactions during the preceding or current calendar year.
- A retailer that has gross revenue from Iowa sales of at least \$100,000 during the preceding or current calendar year, and does one of the following:
 - (a) Owns, licenses, or uses software or data files that are installed or stored on property used in Iowa (including cookies or software that is downloaded as a result of the use of a website);
 - (b) Uses in-state software to make Iowa sales; or
 - (c) Provides, or enters into an agreement with another person to provide, a content distribution network in Iowa to facilitate, accelerate, or enhance the delivery of the retailer's internet site to purchasers.
- A marketplace facilitator that makes or facilitates Iowa sales on its own behalf or for one or more marketplace sellers of at least \$100,000 or in 200 or more separate transactions for the preceding or current calendar year.

- A referrer, if for the preceding or current calendar year, \$100,000 or more of Iowa sales or 200 or more separate transactions result from referrals from the referrer's platform.
- A retailer that makes Iowa sales through the use of a solicitor – a retailer will be deemed to have a solicitor in the state if they have click-through arrangements with in-state residents (however, note that the "solicitor" language appears to be limited to use tax, as it specifically does not apply to sales taxes imposed under Chapter 422).
- A retailer that owns, controls, rents, licenses, makes available, or uses any tangible or intangible property in the state to make or otherwise facilitate a retail sale.
- A person that enters into a contract or agreement with a governmental entity, including contracts for the provision of financial assistance or incentives.
- An affiliate of any person required to collect and remit sales and use tax if the affiliate also makes retail sales.

A marketplace facilitator is any person, including any affiliates of the person, that facilitates a retail sale by: (a) directly or indirectly performing one or more of a series of listed activities related to listing or advertising the seller's products for sale on a marketplace owned or controlled by the person, or accepting or fulfilling orders for the seller's products; and (b) directly or indirectly performing one or more of a series of listed activities related to collecting or processing payment for the seller's products. Under Senate File 2417, a marketplace facilitator that exceeds the sales thresholds is required to collect sales and use tax on facilitated sales, regardless of whether the marketplace seller is registered or would have been required to collect tax on the sale if it was not made through the marketplace.

A referrer is a person that: (a) contracts or agrees with a retailer, seller, or marketplace facilitator to list or advertise items for sale, if the listing or advertisement identifies whether or not the retailer, seller, or marketplace facilitator collects sales and use tax; (b) receives a commission, fee, or other consideration from the retailer, seller, or marketplace facilitator for the listing or advertisement; (c) transfers the customer to the retailer, seller, or marketplace facilitator; and (d) does not collect payments. The term referrer does not include a person primarily engaged in printing or publishing a newspaper, or a person that does not provide shipping terms and does not advertise whether the retailer, seller, or marketplace facilitator collects sales or use tax. A referrer will not be required to collect and remit tax if it complies with specified notice and reporting requirements. These requirements include providing notices to potential purchasers that use tax may be due, notifying sellers to whom customers are referred that they may be required to collect tax and providing information electronically on a monthly basis to the Department on sellers to whom potential customers were referred.

Senate File 2417 gives the Department the discretion to adopt rules imposing notice and reporting requirements for retailers, including marketplace facilitators, that do not collect and remit sales tax and to impose penalties for the failure to comply with the requirements. Adoption of such rules by the Department is not mandatory.

More broadly, Senate File 2417 gives the Director authority to regard any agent or affiliate of a retailer as a retailer for sales and use tax purposes if it is necessary for the efficient administration of sales and use tax requirements. Senate File 2417 also provides that affiliates that directly, indirectly, or constructively control the retailer are jointly and severally liable for any sales tax, penalty, and interest, and provides the Department the discretion to disregard or look through any organizational structure in order to assess and collect tax, penalty, and interest against an affiliate acting to benefit an affiliate or an enterprise of which the affiliate is a part.

Other Sales and Use Tax Changes

Senate File 2417 amends the definition of “manufacturer,” and specifically notes that the term “manufacturer” does not include persons who are not commonly understood to be manufacturers, such as those engaged in construction contracting, repairing tangible personal property or real property, providing health care, farming (including cultivating agricultural products and raising livestock), and transporting for hire. This change takes effect immediately upon enactment of the bill.

Contacts

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