

Iowa Nonconformity: Coronavirus Aid, Relief, and Economic Security (CARES) Act of 2020

(Updated 3/18/21)

On March 27, 2020, President Donald Trump signed Public Law 116-136, the Coronavirus Aid, Relief, and Economic Security (CARES) Act of 2020. The CARES Act includes a number of federal tax changes, and several are retroactive to tax years 2018 and 2019.

Iowa has not conformed with any of these federal tax changes to the extent they apply to a tax year beginning prior to January 1, 2020. Iowa generally conforms with these federal tax changes to the extent they affect Iowa income taxes for tax years beginning on or after January 1, 2020. This guidance focuses primarily on Iowa's nonconformity with this federal law for tax years 2018 or 2019 (i.e. tax years beginning in calendar years 2018 or 2019), but it also includes explanations of certain other provisions and their impact on Iowa income taxes for tax years beginning on or after January 1, 2020 that may be of interest to taxpayers. Not all provisions of the CARES Act are covered by this guidance. Changes in the CARES Act that affect prior year federal income tax payments may affect the computation of the federal income tax deduction or refund for Iowa tax purposes for those years, and are outside the scope of this guidance.

- **Individual Provisions**

2020 Economic Impact Payments under Section 2201 of the CARES Act.

The economic impact payments (EIPs) authorized by section 2201 of the CARES Act, whether they are in the form of a rebate or a refundable tax credit, should not be included when calculating Iowa taxable income for tax year 2020. Additionally, Iowa taxpayers should not include the amount of the EIP as a reportable federal income tax refund for Iowa individual income tax purposes.

- **Business Provisions**

Paycheck Protection Program (PPP) under the CARES Act.

The CARES Act establishes a loan program for qualifying small businesses to incentivize such businesses to keep workers on payroll despite possible financial strain due to the COVID-19 pandemic. Under the PPP, loans may be fully forgiven if the funds are used as permitted under the program. Pursuant to 2020 Iowa Acts, House File 2641, signed by Governor Reynolds on June 29, 2020, a taxpayer's PPP loan that is forgiven and properly excluded from federal gross income under section 1106(i) of the CARES Act in a tax year beginning on or after January 1, 2019, will also qualify for exclusion from income for Iowa tax purposes.

The federal Consolidated Appropriations Act, 2021 (P. L. 116-260) modified the deductibility of expenses paid with PPP loans. Iowa has conformed with the Consolidated Appropriations Act, 2021 for tax years beginning on or after January 1, 2020, but has not conformed for tax years beginning before that date. See Iowa Nonconformity: The Federal Consolidated Appropriations Act of 2021 for more information about Iowa's treatment of PPP loans following the passage of the Consolidated Appropriations Act, 2021.

Modification of certain limitations on charitable contributions during 2020 under Section 2205 of the CARES Act.

Section 2205(a)(2)(B) of the CARES Act provides for an enhanced deduction for qualified contributions made by C corporation, in excess of the regular corporate contribution deduction limitation of 10% of taxable income. Under the new law, a C corporation is entitled to deduct qualified contributions of up to 25% of taxable income. Generally, the qualified contributions must be paid in cash during the calendar year 2020 and the taxpayer must also elect to receive the benefit of the increased charitable contribution deduction under this provision.

Section 2205(b) of the CARES Act provides for an enhanced deduction for contributions of food inventory donated during 2020, increasing the contribution limitation to 25% of applicable income from 15% of applicable income.

Application to Iowa:

Iowa does not conform with the change in section 2205(a)(2)(B) for tax years beginning before January 1, 2020. If a corporation filing on a fiscal-year basis makes a qualified contribution during their 2019 tax year, the taxpayer is subject to the regular corporate charitable contribution limit (10% of taxable income) without regard to the increased limitation and deduction provided in section 2205(a)(2)(B) of the CARES Act. Affected corporations must make required adjustments to their tax year 2019 charitable contributions on the IA 101 Nonconformity Adjustments, line 12. Any contribution carryforward resulting from this nonconformity for Iowa purposes may be deducted in future years on the IA 101 Nonconformity Adjustments, line 12, according to the regular contribution carryforward rules under the Internal Revenue Code. For tax years beginning on or after January 1, 2020, Iowa fully conforms to this additional charitable deduction and increased limitation.

Iowa does not conform with the change in section 2205(b) for tax years beginning before January 1, 2020. If a taxpayer filing on a fiscal-year basis makes a contribution of food inventory donated during their 2020 tax year, the taxpayer is subject to the regular food inventory contribution limitation (15% of applicable income) without regard to the increased limitation provided in section 2205(b). Affected taxpayers must make required adjustments to their tax year 2019 charitable contributions on the IA 101 Nonconformity Adjustments, line 12. Any contribution carryforward resulting from this nonconformity for Iowa purposes may be deducted in future years on the IA 101 Nonconformity Adjustments, line 12, according to the regular contribution carryforward rules under the Internal Revenue Code. For tax years beginning on or after January 1, 2020, Iowa fully conforms to this additional charitable deduction and increased limitation.

Modifications for Wages to which the Employee Retention Credit Applies under Section 2301 of the CARES Act.

The CARES Act created a new Employee Retention Credit (ERC) available to eligible employers against employment taxes equal to fifty percent of qualifying wages of each

employee. The Act further provides that no income tax expense deduction shall be allowed for the portion of wages for which the taxpayer received an ERC for the tax year.

The starting point for calculating Iowa net income is federal taxable income before the net operating loss for corporations, or federal adjusted gross income for individuals. Iowa law contains no specific adjustment for deductions disallowed at the federal level because the taxpayer claimed the federal ERC. Therefore, because no deduction is allowed for wages for which a taxpayer received the ERC at the federal level, no deduction is allowed for these amounts at the Iowa level, even though Iowa has no ERC or equivalent credit.

Modifications for Net Operating Losses under Section 2303 of the CARES Act.

The CARES Act included substantial changes to the federal treatment of net operating loss (NOL) deductions for tax years 2018-2020. Iowa NOLs are calculated independently of federal NOLs, so these federal changes do not directly apply to the Iowa treatment of NOL deductions.

Prior to the CARES Act, under the Tax Cuts and Jobs Act (TCJA), federal NOL carrybacks were only allowed for farming losses and certain other taxpayers for tax years beginning after December 31, 2017. Under the CARES Act, taxpayers must carry federal NOLs arising in tax years 2018, 2019, or 2020 back five years by default, but taxpayers may elect to waive all carryback under IRC section 172(b)(3).

Iowa sets its own carryback and carryforward provisions for NOLs, and these Iowa carryback/carryforward provisions are not directly affected by the federal change. However, Iowa Code section 422.9(3)(c) only allows taxpayers to waive the Iowa carryback period if they also waive the federal carryback period under IRC section 172(b)(3) for the same tax year. As noted on the 2018 and 2019 IA 123 Net Operating Loss (NOL) Schedule instructions, this means that for tax years 2018 and 2019, most taxpayers have no way to waive their Iowa NOL carryback because, under the version of the IRC with which Iowa conforms, there is no federal carryback to waive for those years or the deadline to waive the carryback has passed. In summary, generally only taxpayers with a farming loss may waive their carryback period for Iowa purposes in tax years 2018 and 2019, and may only do so if they timely elected to waive their carryback period for federal tax purposes by the due date of the 2018 or 2019 federal tax return, including extensions.

Accrual basis taxpayers are required to accrue federal income tax refunds resulting from NOL carrybacks or carryforwards to the year in which the NOL occurred for Iowa purposes. See Iowa Admin. Code r. 701—40.18(1)“a”(1), and Iowa Admin. Code r. 701—53.2(1)“a”(1). Taxpayers who amend a 2018 or 2019 federal return to carry back an NOL under the new CARES Act provisions may also need to amend their Iowa returns for that year to account for any refunds received.

2020 Iowa Acts, House File 2641, which Governor Reynolds signed into law on June 29, 2020, allows taxpayers to make an Iowa-only election to waive an Iowa NOL carryback, independent of whether the taxpayer chose or was required to carryback an NOL for the year at the federal level for tax years beginning on or after **January 1, 2020**.

Modification of Limitation on Losses for Taxpayers Other than Corporations (Excess Business Losses) under Section 2304 of the CARES Act.

The federal Tax Cuts and Jobs Act (TCJA) enacted in 2017 created a new provision (IRC section 461(l)) which limited the deduction of excess business losses for non-corporate taxpayers for tax years 2018-2025. This excess business loss limitation is calculated on federal form 461. The CARES Act temporarily suspended this excess business loss limitation for tax years 2018-2020. Iowa is conformed with the CARES Act suspension of the excess business loss limitation for tax year 2020, but not for tax years 2018 and 2019.

- o Iowa treatment for tax year 2018: Iowa was not conformed with the TCJA or the excess business loss limitation for tax year 2018, so the temporary suspension of the excess business loss limitation in the CARES Act should have no effect on the calculation of net income on 2018 Iowa income tax returns. A taxpayer who already filed a 2018 Iowa income tax return prior to the enactment of the CARES Act should not file an amended Iowa return to report a change in Iowa net income solely because of this CARES Act provision. If a taxpayer files an original 2018 Iowa income tax return after the enactment of the CARES Act, the taxpayer should not make an adjustment relating to an excess business loss because of this CARES Act provision on the 2018 Nonconformity Adjustments Worksheet, or on form 2018 IA 1040, line 14, code "m".

NOTE: The excess farm loss limitation under IRC section 461(j) did apply for Iowa tax purposes in tax year 2018, so an adjustment related to that provision may be required on form 2018 IA 1040, line 14, code "m".

- o Iowa treatment for tax year 2019: For tax year 2019, Iowa has conformed with the excess business loss limitation in the TCJA, but has not conformed with the temporary suspension of the excess business loss limitation in the CARES Act. This means the excess business loss limitation will apply for Iowa tax purposes, even though that limitation does not apply for federal tax purposes.

A taxpayer who already filed a 2019 Iowa income tax return prior to the enactment of the CARES Act should not file an amended Iowa return to report a change in Iowa net income solely relating to this CARES Act provision because the excess business loss limitation should already be accounted for on their Iowa return. If a taxpayer files an original 2019 Iowa income tax return after the enactment of the CARES Act, the taxpayer should complete the 2019 federal form 461 (instructions for form 461) to determine whether they are subject to an excess business loss limitation for Iowa tax purposes, even though that limitation does not apply for federal purposes. If the taxpayer computes a negative amount on federal form 461, line 16, that amount should be reported as a positive adjustment on form IA 101 Nonconformity Adjustments, line 12, for tax year 2019. Taxpayers should retain a copy of their 2019 federal form 461 that was computed for Iowa tax purposes. You are responsible for providing documentation at the Department's request to prove your federal excess business loss limitation calculation.

NOTE: The following rules apply when computing the excess business loss limitation for Iowa tax purposes in tax year 2019, and must be considered when completing 2019 federal form 461 and 2019 Iowa income tax returns:

- For tax year 2019, the Department takes the position that deductions under IRC sections 172 and 199A do not apply in the calculation of an excess business loss.
- For tax year 2019, Iowa is not conformed with the technical amendment in section 2304(b)(2)(B) of the CARES Act relating to the trade or business of performing services as an employee. The Department takes the position that for tax year 2019, trade or business within the meaning of IRC section 461(l) can include the activity of being an employee.
- For tax year 2019, Iowa is not conformed with the technical amendment in section 2304(b)(3) of the CARES Act relating to the treatment of capital gain and loss in the calculation of an excess business loss. When determining capital gain/loss

attributable to a trade or business, taxpayers should follow the instructions for 2019 federal form 461, line 11.

- For a married couple who file a joint 2019 federal 1040 but who file separately for Iowa tax purposes, the excess business loss adjustment computed on the 2019 federal form 461 must be divided between the spouses in the ratio of their respective Iowa net incomes (IA 1040, line 26) before application of the excess business loss limitation.
- A nonresident individual, estate, or trust must include the total excess business loss limitation on their IA 1040 or IA 1041. When completing the nonresident credit on the IA 126 or the 1041 Schedule C, the excess business loss limitation addback should be included as Iowa source income in the same ratio that the Iowa business loss (if any) bears to your total business loss.

NOTE FOR TAX YEAR 2020 AND LATER: For federal tax purposes, excess business losses disallowed in a tax year are included in the computation of the taxpayer's federal net operating loss (NOL) carryforward to subsequent tax years. However, Iowa NOLs are computed independently of federal NOLs, and there is no provision in Iowa law that permits excess business losses disallowed for Iowa purposes to be included in the calculation of an Iowa NOL or otherwise deducted in a later year. As a result, excess business losses disallowed (i.e. added back as income) for Iowa tax purposes are not deductible in a later tax year and are lost.

The Department intends to adopt administrative rules as necessary to reflect the excess business loss information in this guidance.

Modification of Limitation on Business Interest under Section 2306 of the CARES Act.

This provision makes several changes to the limitation on the deduction of business interest expense under IRC section 163(j). First, the provision increased the percentage of a taxpayer's adjusted taxable income (ATI) used in calculating the deduction limitation from 30% to 50% for tax years 2019 and 2020. This ATI increase does not apply to partnerships in tax year 2019, and the provision instead includes special rules that ultimately affect a partner's business interest limitation calculation beginning in tax year 2020. Second, the provision permits a taxpayer to elect to use their ATI from tax year 2019 in computing their business interest limitation in tax year 2020.

Iowa is not conformed with these changes to the extent they apply retroactively to a tax year beginning during 2019 (tax year 2019). Specifically, the ATI percentage limitation is 30% for Iowa tax purposes in tax year 2019. A taxpayer (other than a partnership) who does not elect out of this increased ATI percentage provided in the CARES Act must recompute their 2019 federal business interest limitation for Iowa tax purposes using 30% of ATI instead of 50% of ATI. The federal business interest limitation is calculated on federal form 8990.

- Iowa treatment for tax year 2019: A taxpayer (other than a partnership) who already filed a 2019 Iowa income tax return prior to the enactment of the CARES Act using 30% of ATI in their business interest calculation should not file an amended Iowa return to report a change in Iowa net income solely because of this CARES Act provision. However, if that taxpayer later amends their federal return to take advantage of the increased (50%) ATI limitation in their federal business interest calculation, it is recommended that the taxpayer complete the "Tax Year 2019 Interest Expense CARES Act Nonconformity Adjustment Worksheet" in the IA 101 instructions. The results of this worksheet will be used in completing your 2020 Iowa tax return, even though no amended 2019 Iowa

return needed to be filed.

A taxpayer (other than a partnership) who files an Iowa income tax return after enactment of the CARES Act that incorporates the increased (50%) ATI limitation in their business interest calculation must use the IA 101, line 3 to recompute their business interest for Iowa tax purposes using the lower (30%) ATI limitation. For more information, see the instructions to the IA 101, line 3, subline "a".

- Iowa treatment for tax year 2020: Governor Reynolds recently signed 2020 Iowa Acts, House File 2641, which, among other things, decouples Iowa from the IRC section 163(j) business interest expense limitation for tax years beginning on or after January 1, 2020. For tax years 2020 and later taxpayers will be allowed to fully deduct their current business interest expenses for Iowa purposes, regardless of the federal limitation amount. The Department will publish guidance in the near future explaining how to adjust for this nonconformity with IRC section 163(j) for tax years 2020 and later.

Technical Amendments Regarding Qualified Improvement Property (QIP) under Section 2307 of the CARES Act.

This provision modifies the depreciable life of QIP. Prior to the CARES Act, QIP was defined in a manner that classified it as 39-year property for federal depreciation purposes. QIP is defined in IRC section 168(e)(6).

Beginning in tax year 2018, QIP placed in service during the tax year may be classified as 15-year property under MACRS or is assigned a 20-year recovery period under ADS for federal depreciation purposes. Iowa does not conform with this treatment for property placed in service during tax years 2018 and 2019, and instead treats QIP as 39-year property. Bonus depreciation under IRC section 168(k) is not allowed for Iowa tax purposes for any tax year.

- Iowa treatment for tax year 2018: If a taxpayer amends their 2018 federal income tax return after enactment of the CARES Act to reclassify QIP placed in service during that year as 15-year (MACRS) or 20-year (ADS) property, rather than 39-year property, the taxpayer should not amend their 2018 Iowa return because the QIP should already have been properly classified as 39-year property on the original Iowa return. In future years the taxpayer will need to make adjustments on the IA 4562 A/B Iowa Depreciation Adjustment Schedule to account for the difference in allowable depreciation deduction based on the different Iowa and federal class lives for the QIP. For a 2018 Iowa return originally filed after the enactment of the CARES Act, make adjustments similar to those described in the instructions for tax year 2019 below.
- Iowa treatment for tax year 2019: If a taxpayer placed QIP in service and classified it as 15-year (MACRS) or 20-year (ADS) property for federal depreciation purposes, the taxpayer must use the IA 4562 A/B Iowa Depreciation Adjustment Schedule to make appropriate adjustments to treat the QIP as 39-year property for Iowa purposes.

NOTE: Iowa was also not conformed with the classification of certain qualified leasehold, retail, and restaurant property improvements placed in service during tax years 2016 and 2017 as 15-year property for federal depreciation purposes. For Iowa tax purposes, such property was classified as a 39-year property.